

ECONOMIC BASES OF SOVIET POWER

Presented by  
25X1A9a [REDACTED]  
Deputy Assistant Director  
Research and Reports

To  
Mid-Career Course  
School of Foreign Affairs  
Foreign Service Institute  
Department of State  
Washington, D. C.

On  
Wednesday  
19 November 1958

## ECONOMIC BASES OF SOVIET POWER

### Introduction

It seems to me that one of the benefits you might accrue from your course here, particularly since you are not going to remember everything that has been said by all of your speakers, is to uncover sources of information which will be useful to you in your future endeavors; and by sources, I don't mean primary sources, such as foreign publications but, rather, places within the universities and Government, for example, where research materials may be acquired. Therefore, let me say a few words about my own particular organization.

(DCID 3/1, Organization, Numbers, Responsibilities, Samples)

And now as to the substance of this presentation, I think it would be profitable to look first at Soviet objectives as these objectives relate to Soviet economic activity. I think you will agree that most Soviet objectives relate to the accretion of power, both with respect to internal security and the extension of Soviet control over countries outside the Soviet boundaries. This is spelled out very well in Nathan Leites's book which he wrote at RAND entitled "The Operational Code of the Politburo." And certainly Soviet success in the attainment of these objectives rests to an important extent on the economic power available

**SECRET**

to support the main strategy and their day-to-day tactics:

1. One way to accomplish this broad objective would be by direct military action, but hydrogen war seems to be ruled out as a calculated policy for reasons which are well known. Of course, the Soviets must continue to maintain a high level of military expenditures (a) for military preparedness as a deterrent; (b) as a backup for small wars; (c) in an effort to achieve clear-cut military superiority--which, in the minds of the Soviets, would in the future hopefully provide the kind of leverage that they'd like to have to support numerous kinds of blackmail and political threats; (d) the Soviets would need this military power to hold the satellite nations under their domination (as witnessed by their military reaction to the revolution in Hungary and their not very well disguised threats against Poland); (e) and, finally, as we have seen on a number of occasions, this military power is an important adjunct of their control system in maintaining internal security which, we will recall, Khrushchev used very effectively during his short honeymoon with Zhukov. Soviets look to the economy to provide the requisite basis for this military power.

2. A second way in which the Soviets seek to expand their power is to demonstrate internally and for the benefit of the outside world the superiority of the so-called Communist system. On this point, the

economy plays a pivotal role as dramatized, first, by Stalin's and, now, by Khrushchev's promise that the Soviet economy will overtake and surpass that of the United States. Those who have been in the Soviet Union, particularly over the last few years, have been impressed by the extent to which Soviet achievements are accepted as a matter of great pride by people in all walks of life. And the effects outside the USSR are no less dramatic, particularly in the underdeveloped countries where young nations with high economic aspirations are in the process of selecting institutions and social forms as a framework for their future political and economic development. And here, of course, the modified forms of the Soviet system in ~~the~~ Communist China are playing an equally important role as witnessed by the highly publicized contest now in progress between Communist China and India.

3. For reasons of political control and enhanced productivity within the USSR and for the purpose of removing the stigma of poverty which is attached to communism abroad, the Soviets will have to continue to raise the standard of living of the people. This obviously represents another demand on the economy.

4. In order to reduce the problems of Soviet control over the Satellites and to tighten the alignment with Communist China, the Soviet economy is going to have to meet the requirements of the Soviet economic

**SECRET**

Approved For Release 2000/09/01 : CIA-RDP71T00730R000100010005-6

assistance programs for these areas. This has been particularly true with respect to the Eastern European Satellites following the uprising in Hungary.

5. And finally, Soviet political and economic objectives in the underdeveloped countries will require that the economy continue to support its economic offensive in these areas, but more about this this afternoon.

#### The Economic Bases of Soviet Power

Having looked, then, at some of the major objectives of Soviet strategy which rely heavily on the Soviet economy for support, we can turn now to the economy itself. Let me say first that in talking about the economic bases of Soviet power, I don't intend to dwell on Soviet material resources. Suffice it to say that by and large the Soviets have these resources in abundance and in the foreseeable future, these material resources will not represent a critical limitation; rather, I want to put this discussion in the context of the manner in which the Soviets have allocated all of their resources, human and material, and the way in which they focus their economic activity in order to achieve the desired pattern and level of output. We can best begin, I think, by looking at a comparison of U. S. and Soviet GNP.

Approved For Release 2000/09/01 : CIA-RDP71T00730R000100010005-6

**SECRET**

Approved For Release 2000/09/01 : CIA-RDP71T00730R000100010005-6

**(CHART 1--Comparison of US and USSR GNP)**

You can see from the chart in absolute amount Soviet GNP was roughly 40 percent of that of the United States in 1957, but we must understand that this is not an adequate measure of relative Soviet economic strength as applied to its national security policy for a number of reasons.

**(CHART 2--Comparison of US and Soviet GNP by End Use)**

(a) First, defense expenditures were about equal to our own.

This means that if we were to purchase in this country the military goods and services the Soviets are currently buying, it would cost about as much as our own military program.

(b) Second, total Soviet investment--which is the critical element in economic growth--was <sup>(changed)</sup> 67 percent of ours last year and investment in mining, manufacturing, and electric power as 90 percent of that in the U.S., and this year such investment may be equal to ours.

(c) And finally, consumption, or what the consumer gets, was <sup>(changed)</sup> only 31 percent of that in the United States, and on a per capita basis was substantially less than that.

I think it would be useful to examine these three points in somewhat greater detail. If we were to look not simply at defense expenditures

**SECRET**

Approved For Release 2000/09/01 : CIA-RDP71T00730R000100010005-6

but at all expenditures for national policy purposes, we would be even more impressed by the significance of Soviet allocations.

(CHART 3)  
(Briefing Aid--National Policy Expenditures, 1957)

As a preface, let me say that I define national policy expenditures here to include defense, civilian and military research and development, foreign aid, education, and investment in industry. You can see from the chart that (1) Soviet defense outlays in 1957, when converted into dollars, were slightly greater than those of the United States (a rough approximation); (2) Soviet research and development expenditures were in total less than half those of the United States, although military research and development was about two-thirds of ours; (3) our foreign aid program was about four times as costly as that of the Soviets; (4) and that expenditures for education in the two countries were very similar; and here, let me digress for just a second to stress this last point. The emphasis in Soviet education, as you know, is much more on the physical sciences than in our own country. For example, the Soviet Union is graduating about 90,000 engineers a year, compared to our 35,000-40,000. The 10 American educators who recently spent a month in the Soviet Union were amazed by the "degree to which the USSR as a nation is committed to education as a means of national advancement."

**SECRET**

The composition of Soviet investment outlays is also very revealing with respect to the manner in which the Kremlin focuses its resources to meet the political objectives we spoke of earlier.

(CHART 4)  
(Briefing Aid--US vs. USSR Capital Investment, 1957)

This chart reveals a number of interesting comparisons:

1. First, Soviet investment in industry in 1957, which includes mining, manufacturing, and public utilities, was equal to about 90 percent of similar investment in the United States.
2. Second, and in contrast, our outlays for transportation and communications, which includes a massive highway building program, was <sup>nearly</sup> ~~nearly~~ 3 times the comparable Soviet investment.
3. Third, commercial investment, which includes stores, shopping centers, and drive-in movies, was over \$7 billions in the U.S. but only about \$1 billion in the USSR.
4. Fourth, the Soviets put about twice as much money into agriculture as we did, reflecting the neglect of the agricultural sector during Stalin's period and the implementation of Khrushchev's pledge to improve living standards through a better diet.
5. Fifth, our housing investment was about 75 percent higher than theirs, even though living space per capita in the United States is

**SECRET**

well over 4 times that in the USSR. In addition, there are tremendous quality differences here.

6. Finally, <sup>in</sup> "other" investment <sup>much</sup> includes among other things outlays for religious institutions, hospitals, water and sewage and conservation. ~~For these purposes~~, we spent about 2 1/2 times as much as the Soviets.

Summarizing, we can say that the Soviets with a gross national product only about 40 percent of our own have been able to allocate funds to national policy purposes in an amount nearly equal to that of the United States, and here, in my opinion, is the principal economic reason for Soviet success to date.

A few words on the third category which makes up Soviet gross national product, namely, consumption. You may be aware that under the Soviet system, consumption by the population is regarded primarily as a "cost of production" required to insure economic growth, military power, and political stability, whereas in the Western World consumer goods are generally considered to be the principal objective of economic activity. In contrast to the Soviet national security outlays which are nearly equal to our own, Soviet consumption expenditures are only about one-fourth that of the U.S. on a per capita basis. We can conclude from this that in the interest of building Soviet power, it is the consumer

who has had to pay the price. However, two important qualifications should be stressed: (a) The consumer in the Soviet Union has not experienced the standard of living of the Western world, and a steady improvement in these levels of living in the Soviet Union has done a great deal to mitigate potential dissatisfaction; and (b) in the under-developed areas where the Soviets are trying to make an impression with their economic achievements, the population almost universally experiences levels of living below those in the Soviet Union.

(TIME OUT FOR DISCUSSION)

Prospects for Economic Growth

With the background we have just discussed which gives you some idea of the size of the Soviet economy, the pattern of production, and the way in which resources have been allocated to meet Soviet objectives, I think we can now turn to the question of future prospects and here, of course, our estimates are more tenuous but I do feel that the estimates are certainly in the right ball park. Looking back a few years at some of the events which brought us to the present situation, we find that in the period 1953 to 1958, the 5-year period following the death of Stalin, the Soviet economy has undergone a period of experimentation in an effort to unwind itself from the strictures of Stalin's regime

**SECRET**

in an effort to find solutions to some of its basic problems. You probably recall that the first pass in this direction took place during Malenkov's brief <sup>rule</sup> regime when the allocation of effort was to be focused on a higher level of consumption at the expense of defense, and during this period, investment was to be altered in favor of agriculture, light industry, and housing in the hopes of achieving greater industrial productivity and greater agricultural output. With Khrushchev's accession to power, there was an immediate focus in the spring of 1954 on an ambitious agricultural program which, during a 3-year period, was to bring 70-80 million acres of new wheat land into production, to drastically increase corn cultivation, and to launch an extremely ambitious livestock program. Malenkov's consumer goods program was modified to the detriment of consumer durable goods but to the advantage of agricultural output under the new lands program. Housing also continued to be stressed during Khrushchev's early regime, and a greater effort was made to develop incentives through wage reform and higher agricultural prices in order to raise productivity and enhance output. Experiments were also undertaken to improve existing techniques of industrial administration, including planning and control, and although less pretentious than the more recent economic reorganization of 1957-58, these changes seemed to clear the way for uninterrupted

**SECRET**

Approved For Release 2000/09/01 : CIA-RDP71T00730R000100010005-6

pursuit of a new set of 5-year plan goals, goals which were just as ambitious as the Fifth Five-Year Plan. As the Sixth Five-Year Plan got under way, they certainly had every right to expect continued dramatic success but they were very quickly beset by a number of problems that have recently forced them to stop and take stock of a number of undesirable developments.

(a) One of the most worrisome of these problems arose from faulty planning for new plant capacity during the Fifth Five-Year Plan which resulted in the appearance in 1956 of inadequate plant capacities to provide planned rates of growth for certain key industrial raw materials. This under-fulfillment of plans for new plant capacity and the failure to meet production goals in certain key basic industries presented the Soviet leadership with a real dilemma in 1956. Here they were faced with the prospect of continuing to pursue what now appeared to be unrealistic goals during the remainder of the Sixth Five-Year Plan or, as an alternative, the unprecedented abandonment of a five-year plan. Khrushchev's choice was, I think, indicative of his flexibility and willingness to experiment. In brief, he decided to abandon the Sixth Five-Year Plan and to reduce the planned rate of industrial growth for 1957, and in quick succession he undertook, first, to develop a new seven-year plan running from 1959 to 1965; second, to conduct a

-11-

**SECRET**

Approved For Release 2000/09/01 : CIA-RDP71T00730R000100010005-6

SECRET

Approved For Release 2000/09/01 : CIA-RDP71T00730R000100010005-6

sweeping reorganization of industrial management; <sup>To provide</sup> more rapid gains to consumers; and, finally, to change the organization of agricultural production. We'll say more about these last two changes later on, but, first, I would like to focus on the future prospects for economic growth.

The intelligence community believes that the Soviet economy will probably grow less rapidly during the next 7 years than it did during the 7 years previous. (This has been confirmed.) GNP, which on the average has increased about 6.5 percent annually since 1950, probably will grow at a rate of 5.5-6.5 percent during the period 1958-65. At this rate of growth, assuming the United States achieves an annual rate of 3.5 percent, Soviet GNP in 1965 will be about half that of the U.S., as compared with about 40 percent at present.

#### Defense

During this period, as Soviet GNP continues to gain on the United States, the pattern of Soviet expenditures and output by major category will also undergo important changes. In actual amount, the defense allocation by 1965 <sup>on 63?</sup> will be roughly 45 percent greater than the present level. The percentage claim of defense on total gross national product will be about the same, and defense will represent a burden on certain major sectors of industry, such as electronics, since most of the increase will be assigned to aircraft, guided missiles, military research and development, and nuclear weapons.

Approved For Release 2000/09/01 : CIA-RDP71T00730R000100010005-6

Industry

In industry, despite the fine performance in 1957, certain basic industries, particularly in ferrous metallurgy, continued their poor performance largely as a result, as we said earlier, of the failure of the Soviets to provide sufficient productive capacity. Production goals for 1965 in these basic materials suggest that they will receive high priority in order to achieve planned rates of increase. During the Fifth Five-Year Plan, Soviet industrial output increased at the rate of about 11 percent per year on the average, but we presently estimate that the average annual rate of growth under the present Seven-Year Plan is more likely to be somewhere between 8 and 10 percent. (This, too, has been confirmed.) In addition to the constraints involved in their efforts to expand the output of basic materials, the Soviets will be faced with a declining rate of expansion of the labor force. Thus, we have a situation which demands increased output of labor-saving machinery at the same time that raw material supplies are limiting the expansion of machinery output. In summary, it is estimated that the total civilian labor force will only expand by 6.9 million men over the next 7 years, compared to an increase of 9.7 million during the past 7 years. It would appear that the Soviets are looking primarily to agriculture to relieve this dilemma through the transfer of some 3-4 million agricultural workers to industry. This raises the question of

**SECRET**

the prospects for increased agricultural output under a situation which demands that farm workers be transferred to industrial employment.

The Soviets also appear to have recognized this problem and will allocate sizable additional investment to fertilizer production.

25X1X

Agriculture

Khrushchev is well aware that he is flying in the face of the experts with his announced goal of catching up with the U.S. in meat and milk production during the next few years, but he has continued to affirm this program with relatively high levels of agricultural investment. Even so, most experts would agree that the sharp gains made in agriculture over the last few years cannot be maintained. The big impetus to production from the new lands and corn programs were responsible for the substantial increases during the 1953-57 period, but during the next 7 years, total acreage is expected to increase only in an amount equal to about one-fourth that of the earlier period, and new measures must be found if further significant gains in agriculture are to be assured. While the peasants have been given certain income incentives and while organizational changes have taken place in agriculture, we would estimate that the planned increase in agricultural output (7.9 percent <sup>per year</sup>) will be difficult or impossible to achieve with present agricultural programs. In view of the fact that Khrushchev has decided to toss

**SECRET**

SECRET

agriculture into the arena of economic competition with the West, this is an area that may see further innovations in the future that we have not yet identified.

### Consumption

Finally, what are the prospects for the consumer? As in agriculture, it appears that the consumption sector will also not enjoy as rapid an increase over the next 7 years as in the previous 7-year period, but gains will continue to be made and per capita consumption in 1965 may be as much as one-third higher than in 1957; and, in addition, we expect significant improvements in the quality of consumer goods. However, with the possible exception of milk production, we see very little likelihood that Khrushchev can succeed in his efforts to match U.S. per capita consumption of selected food products, <sup>or that the Soviets will match the U.S.</sup> and in other areas of consumption, such as consumer durable goods and housing. ~~Ivan-Ivanovich will continue to lag far behind Joe Doaks.~~ To repeat a word of caution that I voiced earlier, however, the increases in the level of consumption anticipated should be adequate to keep the population reasonably well satisfied with the regime's efforts to improve their well-being.

In summary, we can look for the Soviets to continue to ~~improve~~ improve their relative position with respect to the United States in those areas of the economy which are focused on national security

SECRET

SECRET

objectives. On the question of whether or <sup>when</sup> not the Soviets will catch up with the U.S. in total output, one would need an awfully shiny crystal ball to predict this very precisely. I attended a 3-day briefing presented

a couple of weeks ago where

was giving his estimate on this and he

concluded that it was quite possible the Soviets would catch up with the United States in total output sometime during this century. I have heard others say that this is a conservative estimate and that conceivably the Soviets could catch up with and surpass the United States well before that date. I think it is enough for us to appreciate here that this is a real possibility which must be taken into account in *US security planning*

NOTE:  
a) Depends on US Progress  
b) Discuss in terms of the 7-year Plan

### The Control of the Soviet Economy

Gentlemen, we have talked so far about the economic bases of Soviet power, the growing threat of a rapidly expanding Soviet economy, and I'd like to turn now to one of the most fascinating aspects of Soviet economic development, namely, the way in which this economy is controlled. And while this is a fascinating subject, it seems to me that it is the most difficult to come to grips with because in order to handle it properly, we must consider both the political and economic aspects of this control system, and we must talk about areas which are essentially speculative because the Soviets are going through a fairly dynamic period in the

SECRET

development of their politico-economic system. And I am sure that they are not quite certain themselves just where this will lead. George Kennon, in talking about this subject sometime ago, said that in his opinion the communist system is deeply wrong, that it is wrong about the way the world really works, it is wrong about the importance of moral forces, wrong about human nature, and, in fact, he says it is wrong in its whole outlook. And you know the Soviets have always contended that capitalism bears the seeds of its own destruction, and by this they mean that the capitalistic system can not continue to exist because the conflicts and inconsistencies within the system are irreconcilable. I'd like to suggest that this is more true of the Soviet socialist system than it is of capitalism, and that this system itself bears the seeds of its own destruction. But I think we should clarify what we mean by this. We are not necessarily talking about the disappearance for one reason or another of a Soviet system which is termed state socialism or communism; rather, we are talking about the possibility of fundamental change in this system which would substantially change its identifying characteristics as we know them today. *And I feel that the motivation for these changes will arise from the contradictions among the requirements of what their size does*  
Essentially, the Soviets are looking for a system which will enable the leadership to ~~first~~ *first* develop and maintain a strong centralized control, i. e., control over their own society and over the other nations of the

SECRET

**SECRET**

Sino-Soviet Bloc. Second, they want an efficient and expanding economy, and, third, they want a system that is attractive to the outside world.

Now as to the first of these--the objective of a strong centralized control--they realize that this requires the use of force and repression and rather complete authority over all sectors of the economy. And it also requires a conformance to central authority, at least in the expressed ideas of the people. As to the second objective I mentioned, that of an efficient and growing economy, they recognize here that this requires an educated and a thinking population. Local managers and engineers who have sufficient flexibility to make decisions on their own which, in turn, would argue for a minimum of interference from the party and secret police in the administration of various sectors of the economy. And, finally, in connection with their desire to have a system that is attractive to the outside world, they are well aware that this requires a minimum of repression and coercion, better living standards, and, yet, a continuance of the kind of rapid economic growth that has presented such an attractive image to the underdeveloped countries of the world. Now, I have posed here only three of their major objectives and the requirements to meet these objectives in order to demonstrate some of the fundamental inconsistencies which are inherent in the system. To my mind, these are but a few of the contradictions that they must continually face up to. Some, but obviously not all, of these

**SECRET**

Approved For Release 2000/09/01 : CIA-RDP71T00730R000100010005-6

contradictions have troubled Tito in Yugoslavia and Gomulka in Poland, and their search for solutions have led them in many occasions down quite different paths than those traveled by the Soviet leadership. Up to this point, the Soviets have done a pretty good job, I believe, in maintaining a delicate balance between coercion and force on the one hand and incentive and indoctrination on the other under a system which has certainly permitted them to maintain satisfactory control over the Satellites and over their own society, has permitted striking economic advances, and has enabled them to make remarkable gains in their relations with the underdeveloped countries.

Despite this, Khrushchev seems to be well aware that the system is not operating as well as it might, and he has shown a marked willingness, unlike Stalin, to experiment with new solutions to the problems and contradictions which confront the Soviet system. It is obviously impossible for me to discuss these experiments extensively with you today, but I would like to talk a little bit about the most publicized of the recent changes, namely, the reorganization of Soviet industry and to hear some reaction from you on these developments. The ramifications of these changes have been the subject of considerable discussion in the Free World, and there has been an amazing lack of unanimity as to precisely what these changes mean. There apparently was a growing recognition during the last years of Stalin's regime that the growing

-19-

**SECRET**

Approved For Release 2000/09/01 : CIA-RDP71T00730R000100010005-6

**SECRET**

Approved For Release 2000/09/01 : CIA-RDP71T00730R000100010005-6

complexity of the Soviet economy, particularly with respect to planning and administration, was not adequately met by the existing organization, that there was a need to employ labor and material more efficiently and to use incentives instead of police terror to insure better labor discipline and higher labor productivity. In the 5 years subsequent to Stalin's death, there was a relaxation of police terror and political penalties for economic dereliction, and there were changes in investment priorities which assigned greater resources to raw material industries, to agriculture, and to consumer housing. A concentrated effort was also made to stimulate agricultural output through the virgin lands scheme and to provide incentives to collective farmers. Steps were also taken to give more authority to the union republics in the implementation of planning decisions. In some respects, then, the pronouncements of the December 1956 Central Committee Plenum and the February 1957 Supreme Soviet should not have been a complete surprise. The proceedings of the December 1956 meeting highlighted the fact that certain problems of the Soviet economy were reaching an acute stage including, for example, the lack of adequate capacity for certain basic material production, and it was also clear from the give-and-take of the Plenum meeting that serious disagreements existed between some of the industrial managers and the party bureaucrats. In February 1957, we find Khrushchev launching his reorganization scheme and almost

Approved For Release 2000/09/01 : CIA-RDP71T00730R000100010005-6

SECRET

immediately in the following month pronouncing the details for the reorganization in his famous March theses.

(CHART 5)

(Change in the Economic-Administrative Structure of the USSR)

~~We can see from the chart that~~ This reorganization made a number of striking changes:

*changes in middle level administration*

1. First, the economic-administrative structure of the government was altered by changing the makeup of the USSR Council of Ministers.

*changes in  
USSR Council of Ministers  
composition*

2. Second, by concentrating both long-term and current planning in one organization--the Soviet Gosplan.

3. Third, by changing the functions or abolishing most central ministries. *exceptions* (Chemicals, Transportation, Medium Machine, Building)

4. Finally, by establishing regional councils of the national economy (Sovnarkhozy) which were to direct the activity of the majority of industrial and construction enterprises throughout the country.

Four consequences of this reorganization, I think, deserve particular attention. First, there was a great enhancement of Gosplan's influence in planning and controlling economic activity. All central planning was consolidated in Gosplan, greatly enlarging the role of this

SECRET

~~SECRET~~

Approved For Release 2000/09/01 : CIA-RDP71T00730R000100010005-6

organization in directing the economic activities of <sup>ministries in the</sup> republics, ~~ministries~~, the economic councils, and individual enterprises. Second, the role of the party has also been strengthened, especially at the local level where most economic region boundaries followed existing oblast or republic boundaries and where local party units were assigned control functions. Third, with the creation of some 104 economic regions for the express purpose of improving local administration of the economy, two fundamental questions were raised as to the possible impact of this change. First, would the change result in significantly improved efficiency in the system to the extent that economic growth would be significantly affected? And, second, had this move resulted in a change in decision-making procedures which might have significant politico-economic effects on the Soviet system? It's on the last of these points that speculation has been particularly rampant. I'd like to concentrate on these two questions, bringing in the enhanced stature of Gosplan and of the local party representative <sup>only</sup> in so far as this bears on these questions. In order to determine just what effect this change has had on the efficiency of the Soviet economic system, we should first look at precisely what the Soviets hoped to accomplish through this change. Essentially, it was hoped that reorganization would effectively cure a number of basic problems. I think we might usefully take a look at the more important of these:

Approved For Release 2000/09/01 : CIA-RDP71T00730R000100010005-6

SECRET

1. First, there is the so-called joint products case which, simply stated, outlined their concern with the failure of certain organizations producing particular products to effectively utilize by-product output. In one ore processing plant, for example, only zinc, lead, and copper were extracted, while several other important elements--the responsibility of a different ministry--were discarded as waste.

25X1A 2. Second, is the preoccupation <sup>with</sup> of self-sufficiency which, if you've read [REDACTED] you will recognize has the tendency on the part of individual firms to produce items which could be subcontracted more efficiently. In the minds of the individual managers, this was done for a good reason. ~~This was considered an essential undertaking, since~~ <sup>largely because</sup> the whole success of <sup>the managers</sup> ~~this~~ operation rested on <sup>this</sup> ~~their~~ ability to meet planned goals. Subcontractors were often not reliable in delivering the amount, kind, and quality of the items desired. Hence, the motivation by individual plants to produce a number of these items themselves.

3. Third, there was the much publicized point of cross-hauling, which can be simply stated as carrying coals to Newcastle. In one example cited, a construction trust located in Karaganda imported bricks from Ust-Kamenogorsk even though there was adequate capacity from <sup>nearby</sup> ~~the~~ Karaganda kilns of a construction trust belonging to a different ministry.

SECRET

25X1A

4. Fourth, there was another problem that the readers of [REDACTED] will recognize, namely, the hoarding of surplus inventory which is the practice of storing reserves of various materials and components in excess of legal requirements. This, it seems to me, is a perfectly normal offshoot of the kind of system that the plant managers find themselves in. <sup>Since</sup> ~~in order to insure that~~ production, which is the do-all and

end-all of success as measured by Soviet criteria, <sup>The manager does not let production</sup> ~~will not be interrupted~~

<sup>be interrupted</sup> by ~~the~~ inability to obtain critical manufacturing inputs. This was the managers' so-called "safety factor."

5. Fifth, it was contended that there was considerable duplication in administrative overhead. In the Gorky Oblast, for example, lumber procurement was handled by <sup>some</sup> ~~40~~ ministries and individual agencies.

6. Sixth, there was a lack of the joint use of basic resources reflected by situations where an enterprise vertically integrated would have exclusive control over a source of raw materials or a source of power which could have been used more effectively by a number of plants under a non-exclusive arrangement.

7. And, finally, there were a whole raft of problems which arose from investment ~~wast~~ waste in planning and plan implementation which involved a number of difficulties too lengthy to recite here. Suffice it to say that it was hoped that the reorganization would promote a more

SECRET

rational allocation of investment funds through greater authority on the part of the economic councils to identify needed investment at the local level. I recite all of these points not merely to show the problems which the Soviets hoped to cure by the reorganization but to show you the kinds of inefficiency and contradictions which are inherent in the Soviets' economic system.

Over the ~~past~~<sup>past</sup> year, specialists in the State Department and in CIA have been examining available evidence to determine to what extent the Soviets have succeeded in eliminating these problems through the reorganization and to what extent the gains in efficiency under the new system might have a significant impact in promoting Soviet economic growth. In the short time we have available here, I think we can only say that they have concluded that the gains have been relatively small and that new ~~problems~~<sup>headaches</sup> of a different kind, such as the preoccupation with local problems, have arisen. Finally, just a few words as to what impact all of this has had on the decision-making process. There has been a great deal of speculation that the reorganization would result in considerably more influence for the economic bureaucrats and the plant managers at the expense of party control at the center. This same State/CIA report which I mentioned earlier looked at this question in considerable detail in terms of the kinds of decisions which are critical in the management of the Soviet economy. These included decisions with respect to investments,

SECRET

**SECRET**

Approved For Release 2000/09/01 : CIA-RDP71T00730R000100010005-6

wages, working capital, distribution of output, planning, and the success indicators at the ~~enterprise~~ enterprise level.

The results of this investigation would seem to support the old French political dictum--the more things change, the more they stay the same. In the area of investment planning and ~~planning~~ implementation, it was found that decisions remain as before in the hands of the central authorities. Local authorities continued to decide the use of a small segment of investments but this authority had, in fact, been granted before the reorganization. The so-called rights given to the economic councils have added very little to this. The initial delegation of limited authority to the councils was severely circumscribed by central controls. During the first year under the new system, there were further restrictions placed on this authority.

Wage rates and total wage funds for the Sovnarkhozy and their enterprises continued to be set by Gosplan in consultation with the State Committee on Labor and Wages.

In the use of working capital, the councils seemed to have less freedom to maneuver funds among its enterprises than had the former ministries.

~~The new supply system has also not added significantly to the authority of the enterprise manager and the councils of national economy.~~

**SECRET**

Approved For Release 2000/09/01 : CIA-RDP71T00730R000100010005-6

**SECRET**

Approved For Release 2000/09/01 : CIA-RDP71T00730R000100010005-6

The new supply system has also not added significantly to the authority of the enterprise manager and the councils of national economy. The enterprise managers still require an allocation order to purchase materials and these orders are intricately tied to the output and supply plans of the enterprise, both of which are ratified from above. There was, you will recall, a lack of certainty in the timely delivery of supplies which, along with a persistent pressure for increased output, had formerly required that the enterprise manager became more self-contained. This situation has changed under the reorganization, and the enterprise manager is more assured of receiving supplies from other enterprises within the same council of national economy. However, this has resulted in a new problem, namely, that enterprise managers are not assured of receiving supplies from enterprises in other economic regions, and the government has had to set up penalties for failure of supplying enterprises to meet external requirements.

All of this raises the question as to the climate of decision-making which surrounds the manager of individual enterprises. From the preceding discussion, I think we can safely conclude that there really has been little change in the rules of the game, that is, the spectrum of choice has not significantly widened. I think this is particularly clear when we consider that the chairmen of the economic councils and

**SECRET**

Approved For Release 2000/09/01 : CIA-RDP71T00730R000100010005-6

SECRET

Approved For Release 2000/09/01 : CIA-RDP71T00730R000100010005-6

the managers of individual enterprises lack the kind of objective criteria which would be essential if they were to have any real latitude in decision-making. There is, of course, the criterion of planned goals, but there are no meaningful criteria which would enable these chairmen and managers at the local level to determine how the available inputs should be most effectively combined in achieving these goals. It is true that the council chairmen, since they are on the spot, may be able to exercise better control over the product mix, that is, the specific grades and quality of output required by the plan, and that these chairmen may also reduce the degree of ignorance in the controlling of individual enterprises which existed when control was exercised in the extreme by the chief directorates and ministries located in Moscow. Despite this, it is very clear that decision-making for all practical purposes still rests at the center.

Having said all this, I am personally not convinced, nor are many others, that the situation has remained essentially unchanged. Moreover, I am convinced that further major experiments are in the offing. The growing education of the populous, the increasing competence and pride of individual plant managers and industrial bureaucrats and their growing resentment <sup>toward</sup> untutored outside interference, the growing complexity of the economy and the need for greater efficiency, the relaxation of

-28-

SECRET

Approved For Release 2000/09/01 : CIA-RDP71T00730R000100010005-6

SECRET

secret police control and the strong aversion to its restoration, all seem to argue, in my mind, that the economy will be directed in the future in a different climate and under changing ground rules. It's not enough to say that control from the center will be assured under the reorganization by local party control. Intuitively I feel that the success of the local party officials depends to an important extent on the success of the local plant managers and the local Sovnarkhosi chairmen and that, in a sense, ~~they~~ <sup>the local party officials</sup> are prisoners of these industrialists because of this dependence. Indeed, there have already been complaints from Moscow of collusion between ~~the local party~~ <sup>these</sup> officials and ~~some of these people~~ <sup>the local economic direction</sup>.

7. (Analogy with "The Last Hurrah") ?

There has been a great deal of speculation on this. Alec Nove, the British economist and Sovietician, has suggested that costs and prices could conceivably become more dominant as criteria in economic management at the lower levels. And certainly, though the analogy is strained, Oscar Lange, one of the principal economists in Poland, seems to be pushing the Poles in this direction, however feebly. So, in conclusion, I <sup>would</sup> ~~might~~ say that my intuitions about the contradictions within the Soviet system would argue that important changes are still in the offing.

SECRET

SECRET

Afternoon Program at FSI

25X1A

Approved For Release 2000/09/01 : CIA-RDP71T00730R000100010005-6

The Soviet Economic Offensive

I am sure you are all aware of the statement Khrushchev made sometime ago declaring war on the United States in the field of peaceful trade. And it's pretty apparent that this is no hollow threat. However, it doesn't tell the full story, since this desire to compete in international trade--which has been termed the economic offensive--is simply one weapon in the arsenal of political, military, and economic weapons which are all designed to support Soviet foreign economic policy in its drive for greater power beyond its borders. This economic offensive supports the Soviet drive to increase Bloc prestige and influence in the uncommitted countries which, in its early stages, involves the encouragement of neutralist policies in these countries and the lessening of Western influence. So we can say at the outset that these economic activities, while they have unquestionably provided economic gains to the Bloc, are really undertaken primarily for political purposes.

I think it's important to look first very briefly at two other aspects of Soviet international economic relations. First, total exports of the USSR in 1957 totaled about \$4 billion. This, parenthetically, compares with \$18 billion in U.S. exports, and, significantly, of the \$4 billion in Soviet exports, only about 25 percent go to the Free World. This means, of course, that the bulk of the Soviets' trade is with other countries of

SECRET

Approved For Release 2000/09/01 : CIA-RDP71T00730R000100010005-6

SECRET

Approved For Release 2000/09/01 : CIA-RDP71T00730R000100010005-6

the Sino-Soviet Bloc. Over two-thirds of this trade with the Bloc is with the European Satellites, and the balance is with Communist China. Similarly, the bulk of Soviet credits -- 78 percent -- have been extended to the Bloc countries over the past 8 years. The second important fact is that in its economic relations with the Free World, roughly 15 percent has been with the industrialized nations of Western Europe, as opposed to 10 percent with the underdeveloped countries. And, unlike the trade with the underdeveloped countries, trade with Western Europe is based primarily on economic motivations. Now on this point there has been a great deal of discussion recently in connection with the Soviet invasion of important Western commodity markets, such as their highly publicized exports of aluminum and tin, and there has been considerable disagreement as to whether this activity is primarily based on political rather than economic objectives. It has been argued that these exports of aluminum and tin have been designed to disrupt Western commodity markets, and that the Soviets have been engaging in uneconomic price manipulation. We and the State Department experts have concluded, however, that for the most part the recent price cutting of the Soviets in the sale of these commodities has been designed to facilitate sales which will yield them the foreign exchange necessary to pay for Bloc imports from the West. We can talk about this a little more if you have questions on this point.

-2-

SECRET

Approved For Release 2000/09/01 : CIA-RDP71T00730R000100010005-6

**SECRET**

Approved For Release 2000/09/01 : CIA-RDP71T00730R000100010005-6

With this background, I think we can examine the Soviet economic offensive in the underdeveloped areas by answering two questions. First, what is the nature of the offensive, that is, what does it consist of? And, second, what is the impact of this offensive? The Soviets in carrying out this program have drawn on the resources of the entire Sino-Soviet Bloc. This is not to say that all Bloc economic relations with the uncommitted countries are tightly coordinated from Moscow and that each transaction is directed by the Kremlin. However, we can say that the activities of the entire Bloc in this field do support Soviet objectives, and we could not sum up the political advantages to the Soviet Union in any meaningful way unless we looked at the activities of the Bloc as a whole, so for the balance of this discussion we'll be talking about the Bloc rather than simply the USSR. Very briefly we can outline these economic activities under the headings of (a) credits and grants, (b) trade and trade agreements, (c) the export and training of technicians and professional personnel, and (d) related activities.

(CHART--Bloc Extensions of Credits)

Credits and Grants

Since this program really got under way in 1954, Bloc military and economic credits and grants to the underdeveloped countries have totaled

**SECRET**

Approved For Release 2000/09/01 : CIA-RDP71T00730R000100010005-6

over \$2 billion. By 30 June 1958, over \$1,300,000,000 of these credits had been obligated and over \$700 million had actually been drawn. The Soviets alone had extended over \$1,200,000,000 of the total credits and had actually delivered over \$300 million. Of the total \$700 plus million which had actually been drawn on by the uncommitted countries, over \$400 million has been used to finance the purchase of arms. (Prices favor underdeveloped countries.) Generally speaking, Soviet credits have involved interest payments of 2 1/2 percent and have usually run about 12 years. Satellite credits have been a little more expensive, costing about 3 percent (sometimes as high as 5-6 percent) and running on the average somewhat less than 12 years.

Second, a small number of countries have been the principal recipients of these credits: Egypt, Syria, Yemen, Afghanistan, India, Indonesia, and Yugoslavia.

In connection with these credits, one of the principal controversies centered around the question of Soviet capabilities. It has been argued that the Soviets with declining rates of industrial growth, with the necessity for providing economic credits to the Satellites, are not in a position to significantly expand this assistance and, indeed, that this assistance represents a sizable burden on the Soviet economy. I think we can dispense with this argument fairly quickly by pointing out that

Soviet gross national product in 1957, as we discussed it this morning, totaled roughly \$120 billion, and if we look at the chart, we can see that to date through the entire course of this program over a 4-year period, the drawings against Bloc credits have only totaled something over \$700 million, of which only \$300 million was Soviet; and even if we assume that some of the economic credits to Egypt were in fact Soviet credits, the annual burden on the USSR has probably not been much more than \$100 million a year and that, moreover, these are credits, not grants, which presumably will be paid back, at least in part. The argument as to the limited ability of the Soviets to extend such credits was an important question within the U. S. Government a couple of years ago, and we argued that the Soviets would always match the economic cost involved against the potential political gains; and it was shortly after this that the Soviets extended several significant additional credits to Syria, Egypt, and Indonesia. Needless to say, we still adhered to our original position on this.

*NOTE:  
Info  
on drawings  
not satisf.*

#### Trade and Trade Agreements

(CHART--Bloc Trade with Underdeveloped Countries)

In 1954, Bloc trade with the underdeveloped countries was some \$870 million; in 1957, it was roughly double that amount, and it is

SECRET

SECRET

Approved For Release 2000/09/01 : CIA-RDP71T00730R000100010005-6

*NOTE.*

*a) little increase in '58  
b) M.E. up  
c) depressed commodity  
export prices may be cause*

significant that the bulk of Bloc trade with the uncommitted nations was in SEA focused primarily on the more politically vulnerable countries of South And Southeast Asia and the Middle East. I think it's also interesting to note that this trade has reached the point where it represents a significant percentage of the total trade of a number of the underdeveloped countries-- Afghanistan, roughly 40 percent; Egypt, 36 percent; Iceland, 33 percent; Syria, 12 percent and growing rapidly--and that this trade has been stimulated in no small part by the extension of Soviet Bloc credits. ~~This increase in trade has also been accompanied by a very sharp increase in trade agreements.~~ Not only have the Soviets been selective with respect to individual countries which have become the focus of Soviet trade ~~xxxx~~ activity, they have also been very perceptive in concentrating on the import of products which represent burdensome surpluses in these countries and which have also taken a political significance. These include the import of rubber from Ceylon, cotton from Egypt, fish from Iceland, and rice from Burma, and wool from Uruguay.

#### Technicians

(CHART--Bloc Economic and Military Specialists in Underdeveloped Countries)

You can see from the chart that the pattern of Soviet specialists in underdeveloped countries follows pretty much the pattern of its trade

Approved For Release 2000/09/01 : CIA-RDP71T00730R000100010005-6

and credit program, with such politically vulnerable countries as Egypt, Syria, Afghanistan, Yemen, and Indonesia representing important targets. Altogether in the ~~px~~ period 1 January to 30 June 1958, there were roughly 3700 of these specialists in the underdeveloped countries, and this is, of course, a minimum figure. (~~Do we know how many from the Free World?~~) Roughly 2600 of these were economic specialists of one kind or another, and the balance were military personnel, and this doesn't tell the whole story. Since 1955, over 2,000 <sup>students and</sup> military trainees and students from the underdeveloped countries have been sent to the Bloc for training and, of these, about 500 have enrolled for advanced training in universities and other Bloc institutions; 700 Indians alone have been scheduled for training in the Soviet steel works. This, of course, represents an additional danger to the Free World. If you'll recall, Tito at the time of his first break with the Soviet Union complained bitterly in his White Paper that the Soviets made definite efforts to subvert some of the Yugoslavs who had been sent to the Soviet Union for training. Another important thing to keep in mind here, and this is somewhat in contrast, is that the Bloc specialists who have been sent to the underdeveloped countries have given a very good account of themselves and, by and large, though there are some exceptions, they have stuck strictly to their jobs and have not engaged in subversive activity. Moreover, many

**SECRET**

of these specialists have had training in the language and customs of the areas to which they have been assigned and this, of course, appeals to the pride of the local nationals. If you've read accounts of the recent book, "The Ugly American," you know precisely what I mean.

Other Activities

There have been other devices which the Bloc has used to achieve their purposes and these include elaborate participation in local trade fairs, local commercial advertising, extensive use of local trade representatives and missions, and elaborate propaganda dramatizing the success of the Soviet economy and the benefits to be derived from the adoption of the Soviet brand of state socialism. One other device which I'd like to <sup>comment</sup> pass on was brought home to me in a recent trip I took <sup>the SEA</sup> around the world when I learned of the activities of the Chinese Communist Bank of China. This bank has branches throughout Southeast Asia which not only provide a source of funds for both overt and covert programs which the communists are seeking to support but also provide a source of leverage and pressure against the local Chinese communities. These branches provide loans to local merchants which, in turn, enables the communists to pressure these local Chinese into such activities as sending their children to Chinese Communist schools, flying the Chinese Communist flag on appropriate holidays, and undertaking certain other covert and overt activities which benefit the Chinese Communists.

**SECRET**

SECRET

Approved For Release 2000/09/01 : CIA-RDP71T00730R000100010005-6

(TIME OUT FOR QUESTIONS)

Impact of the Soviet Program

It has been a great mystery, I think, to many people as to how it is that the Soviet penetration program could have reached its present level of success with such a relatively small expenditure of resources. After all, the amounts involved are not large compared with the expenditures of the United States and, in most instances, the economic impact has been small compared with the total output in the individual underdeveloped countries concerned.

I had some difficulty trying to decide how to present this picture of the impact of the Soviet Bloc program because there are two points which should be stressed. First is the question of what the Soviets are trying to achieve, and second, there is the question of how it is they are doing it so effectively. As a matter of presentation, I have decided to talk about their objectives and in the course of this, we can look at some of the ways in which they have run the program. And let me say that in discussing these various categories of objectives, I don't mean to imply that these are clear-cut and exclusive of one another but I have simply adopted this tack as a matter of convenience.

To Gain a Position of Respectability, Prestige,  
and Diplomatic Influence

In order to gain a better climate for Soviet diplomacy and for the

SECRET

Approved For Release 2000/09/01 : CIA-RDP71T00730R000100010005-6

**SECRET**

local communist parties, the Soviets have sought to gain a position of respectability and prestige through the economic penetration program, and they have done this in a number of ways. First, they have made considerable progress in dispelling the image of communism as an aggressive force by appearing to show a deep concern for the independence and for the economic and political aspirations of the uncommitted nations. They've done this by extending economic aid which, as you have heard many times, ostensibly has no strings attached and does not require military agreements. They have stressed over and over again through all their propaganda media that they seek to promote the economic well-being of these countries, and they make a great point of contrasting this with the so-called exploitation of the colonial powers.

They have not been averse to the so-called "impact" projects which in many ways are uneconomic in that they represent an inefficient allocation of resources in the underdeveloped countries. Nevertheless, the Sports Palace in Burma and the famous asphalt streets in Afghanistan are the kinds of showpieces which make political capital for the communists. Whether this may come back to haunt the Soviets later on is another question. Of great advantage has been their show of flexibility and the speed with which they are able to react to given political opportunities and the promptness with which they are able to make deliveries

**SECRET**

**SECRET**

Approved For Release 2000/09/01 : CIA-RDP71T00730R000100010005-6

when such promptness is important. At the time Ghana was celebrating its independence, the Soviets chose that opportunity to make dramatic purchases of cocoa. When surplus Sudanese cotton became a hot local political issue, the Soviets offered to purchase this cotton on terms very favorable to the Sudanese. When Iceland was unable to market its fish in the West, the Soviets stepped in to purchase large quantities of this surplus. This kind of opportunism makes a tremendous impression in the countries concerned. And if the Soviets find that something has gone wrong with a particular transaction which is a source of irritation in a country, they are very quick to move in and make adjustments. Burma, you will recall, built up a large credit balance as a result of its agreement to sell rice to the Soviets; and they were unable to make arrangements for appropriate purchases of Soviet exports in exchange and the Soviets, with a great show of good will, permitted these credits to be used in purchases from Eastern Europe. Finally, it has been very clear that Soviet technicians abroad have been building good will for the Bloc, and, as I said earlier, they have been able to do this in part as a result of training in the customs and language of the country to which they are assigned, and, second, by behaving themselves and by not living ostentatiously in the midst of local poverty.

There have been occasions, of course, when the Soviets have been

-11-

**SECRET**

Approved For Release 2000/09/01 : CIA-RDP71T00730R000100010005-6

SECRET

hoisted on their own petard. When political difficulties arose with Yugoslavia, they were forced to reveal the hidden strings to their aid agreement when they walsed on certain promised deliveries. The aura of respectability which they have tried to build up was also tarnished to a considerable extent by their military action in Hungary which, for the moment at least, made countries like Iceland and Indonesia much more leery of communists bearing gifts. In general, however, we'd have to say that the Bloc is gaining prestige and respectability through the <sup>from</sup> offensive, that their diplomats are finding more doors open, and that in many cases, new missions are being established which give the Soviets more opportunity for influence. I recall on a trip to Latin America in 1956, we were told by the Uruguayans that because the West wouldn't buy up their surpluses, they were being forced to trade with the Soviet Bloc and that as a result, they were permitting increased Bloc representation in their countries. The Bloc has had considerably less success in facilitating the activities of local communist parties through this "soft sell" approach. As you know, Nasser, ~~K~~ Nehru, and Frondizi are all giving the communists a hard time, although in places like Indonesia the communist party has probably gained as a result of the Bloc's political and economic activities there. In general, I think we'd have to say that the Soviets are succeeding in very dramatic

*NOTE: Recent reports of Sov. dumping here also hurt Sovs.*

*though*

SECRET

**SECRET**

Approved For Release 2000/09/01 : CIA-RDP71T00730R000100010005-6

*Program*  
fashion in this ~~objective~~, and, in my opinion, I think this beneficent attitude which the Soviets are showing toward the underdeveloped countries is probably as important as any single effort they have made to extend their influence in these areas.

#### Exploitation of Troubled Situations

Whenever local disputes arise in an area or ~~whenever~~ whenever conflicts between uncommitted countries and the West appear, you can be certain that the Soviets will be giving the situation a good hard look to see how they might exploit these developments. The Arab-Israeli dispute, the Afghan-Pakistan disagreements over the Pushtoonistan area, the Suez crisis, and Yemen's conflicts with the British are all clear ~~examples~~ examples of this. Local armed conflict is often to the advantage of the Soviets, and when this is the case, they seek to aggravate rather than ameliorate these situations. Bloc arms shipments to Egypt and Syria were clearly intended for this purpose as well as the advantages these shipments have had in appealing to local nationalism. When Afghanistan shipments through Pakistan were halted, the Soviets also delivered arms to Afghanistan and gave Afghanistan transit rights through the Soviet Union. ~~The Bloc arms shipments to Yemen fall in the same category.~~ This kind of economic aid is not costly, particularly when relatively obsolete arms are delivered, though we should be cautious on this point because in many instances the military equipment supplied has been reasonably modern and up to date.

Approved For Release 2000/09/01 : CIA-RDP71T00730R000100010005-6

Selling the Soviet System

A great deal has been said about the contest between the Soviet Bloc and the Western World in their respective efforts to sell state socialism and a free economic society. Soviet advisers, technicians, diplomats, and visiting lecturers are pressing hard in this arena through their efforts to live up to contract agreements, to meet the requirements of the local economies, and to publicize the image of successful Soviet economic systems, ~~within the Bloc~~. The contest between India and Communist China, I am sure, is well known to all of you. The underdeveloped countries would all like to make the kind of quantum jump which they have seen in the Soviet Union and which they have appeared to be witnessing in Communist China. The Soviets lose no opportunity to stress the fact that they, too, were a backward country some 40 years ago. The arguments of the West which recite the tremendous human cost are not as impressive to the underdeveloped countries as they would be in an industrialized society. And Khrushchev in his recent theses on the Seven-Year Plan has even sought to remove this ~~st~~ stigma. In pursuing this objective, the Soviets are providing technical assistance and training personnel for nuclear energy experimental laboratories (Egypt), they are establishing and staffing technological institutes (Bombay and Rangoon), they are providing scholarships for study in

**SECRET**

major Bloc universities and technological institutes, and they are providing planning experts on a consultative basis in Egypt and India. It has been particularly difficult to determine the extent of Soviet success in selling their system. Thus far, the evaluation of its impact has been particularly elusive, but this much we can say, the Soviets have unquestionably gained leverage in the pursuit of this objective, and it's an effort that must be countered by the West.

The Collection of Intelligence and Subversive Activities

It seems clear that at this stage of the Bloc program, the collection of intelligence and the undertaking of subversive activity is not a major element of the program. I say at this stage because the principal objective of the Soviets at this point is to substitute Soviet influence for that of the Western World. They are generally not concerned at the moment with open take-over of these countries. There, of course, may be exceptions to this but it seems clear if they were caught in the act in an effort to undermine an underdeveloped nation with a clear purpose of bringing it under Soviet domination, they would lose the tremendous advantages they had gained in other countries throughout the area. We are aware of instances where trade missions have ~~taken~~ included personnel with intelligence collection missions. We do know that a Soviet vessel assigned to pick up Cuban sugar was fully equipped

with electronic gear to monitor activity at the U.S. Naval Base at Guantanamo, and we had some very pregnant suspicions about the objectives of the Czech bid to install telephone equipment in Uruguay. Moreover, we are very clear that the activities of the Bank of China, as I told you earlier, are not confined to financing Chinese Communist trade. This kind of activity obviously requires close surveillance and counter-measures but we should not be deluded into thinking that this is a major objective at the moment of the Bloc's economic offensive.

In summary, we can say that the Soviets are seeking to pursue their objectives through a skillful combination of political and economic maneuvers which have been characterized by:

- (1) Prompt exploitation of political opportunities;
- (2) Brief periods of negotiation, flexibility in meeting the demands of underdeveloped countries, and, where necessary, prompt delivery;
- (3) Simultaneously integrating their response to a number of the main requirements of the underdeveloped nations. This includes their willingness to discuss a line of credit, the specific imports required, the technical assistance needed, and the disposal of exportable surpluses in these countries. And I'd like to stress here that this has a great appeal and is one of the most effective aspects of the Soviet program. When Sudan was unable to market its cotton, the Soviets went in and offered all of these things I have just referred to simultaneously--

**SECRET**

they offered to take a large part of Sudan's cotton surplus, they offered to provide the imports required for Sudan, and they offered to provide economic and technical aid. This is very hard to resist, particularly when the local leaders are being pressed by the opposition.

(4) Another characteristic of the Bloc program is that it is handled almost entirely through credits, with practically no grants except in the case of Communist China. Interest rates are low, at roughly 2 1/2 percent; repayment usually begins after the project is in operation; and the amortization period usually runs *about 12 years.* ~~from 20 to 30 years.~~

(5) Bloc loans generally cover only foreign exchange costs, although even here they have shown great flexibility recently in agreeing to provide for some of the local costs as well in Afghanistan.

(6) Most assistance is related to industrial development. This is a point we have not covered earlier but it is significant that most loans are for sugar mills, cement plants, steel plants, etc., and not for sanitation, sewage, housing, etc.

(7) Trade and aid agreements are independent of military pacts and, while the Bloc has provided arms on credit, no underdeveloped country receiving Bloc military or economic assistance is a member of a Bloc military alliance. This has been a very disarming practice on the part of the Soviets.

There is no question that the Soviet program has been inexpensive and successful, and this <sup>success</sup> ~~subject~~ has, in my mind, been largely attributable to clear understanding of local conditions and great flexibility in exploiting these conditions.